

COMMONWEALTH OF KENTUCKY
BEFORE THE PUBLIC SERVICE COMMISSION

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In the Matter of:

AN ADJUSTMENT OF RATES OF ROLLING)
HILLS SERVICE COMPANY, INC.) CASE NO. 7983

O R D E R

On September 30, 1980, Rolling Hills Service Company, Inc., ("Applicant") filed an application with this Commission giving notice of an adjustment of rates to become effective December 1, 1980. Applicant stated that the proposed rates would result in additional annual revenues of \$56,717. However, after considering the annual revenue based on the consumers at the end of the test period the increase in revenue would amount to \$47,710 annually or 25%. By Commission Order, the effective date of the proposed tariffs was suspended for five months pursuant to the provisions of KRS 278.190.

On October 7, 1980, the Division of Consumer Intervention in the Department of Law filed a motion to intervene in this proceeding. The city of Rolling Hills filed a motion to intervene on January 9, 1981. These motions were sustained and both parties participated in the proceedings. A hearing was scheduled January 14, 1981, at the Commission's offices in Frankfort, Kentucky. All parties were notified in manners prescribed by Kentucky Revised Statutes and Commission Regulations, and the hearing was conducted as scheduled.

On February 23, 1981, the intervenors for the city of Rolling Hills filed a motion requesting another hearing to put on proof and to rebut the allegations of the Applicant. The hearing was scheduled for April 14, 1981. The Applicant failed to have a key witness available for cross-examination at this hearing. Therefore, the Commission issued interrogatories in order to obtain the information needed from the witness. On May 8, 1981, the Applicant filed its response to the interrogatories and a second set of interrogatories was served on May 21, 1981, in that the first set was insufficient.

On March 9, 1981, the Applicant filed a waiver of the five-month suspension period and the ten-month statutory period for a period of 30 days. On May 20, 1981, a waiver for an additional 30 days to July 1, 1981, was filed and sustained by the Commission. Another waiver of the suspension period was obtained through July 23, 1981, and the ten-month statutory period. The matter of the proposed increase in rates is now considered submitted for final determination by the Commission.

Commentary

Rolling Hills Service Company, Inc., is a privately owned sewage treatment system serving approximately 1368 customers in eastern Jefferson County, Kentucky. Rolling Hills Service Company is operated by Rolling Hills Operating Company ("Operating Company"). The Applicant and Operating Company are owned by George Martin, Campbell Miller, Benjamin Wihry and Jesse Bolinger.

Both of these businesses are conducted from the offices of Miller, Wihry and Lee, an engineering firm. Benjamin Wihry and Campbell Miller have ownership in all three businesses. Miller, Wihry and Lee performs the bookkeeping and engineering services for the Applicant. Woodrow Smither, Vice President of the Operating Company and an engineer of Miller, Wihry and Lee, overlooks the operations of the Applicant. Mr. Smither also performs professional engineering services for the Applicant which are billed directly on an hourly basis.

Test Period

The Commission has adopted the twelve-month period ending June 30, 1980, as the test period for the purpose of determining the reasonableness of the rates approved herein. Pro forma adjustments have been included where found reasonable and proper for rate-making purposes.

Revenues and Expenses

Applicant proposed several adjustments to revenues and expenses as reflected on its Comparative Income Statement, Exhibit 10. The Commission is of the opinion that the proposed adjustments are generally proper and accepted for rate-making purposes with the following modifications:

(1) Applicant proposed an adjustment of \$1,323 for increased sludge hauling expense. The Rolling Hills Operating

Company, operator for the Applicant, was charging the Applicant a 25% markup on this expense which was directly sub-contracted by Rolling Hills Operating Company. At the hearing of April 14, 1981, the Applicant testified that they were no longer being charged a markup on this expense from the Rolling Hills Operating Company. Therefore, the Commission has reduced the test year expense by \$3,841 to an adjusted amount of \$25,755. The adjusted amount is based on the actual test year experience of 255 loads, at a current cost of \$101 per load.

(2) During the test year , Applicant incurred \$19,733 in equipment lease expense. Included in the test year expense were two leases expiring on February 28, 1981, and January 5, 1983. The Applicant used an average of the two leases to arrive at an adjusted expense of \$9,615. This resulted in a reduction of \$10,118 to the test year expense. However, the Commission is of the opinion that none of the expense associated with the lease which expires on February 28, 1981, should be included for rate-making purposes in that this cost will no longer be incurred. This results in a further reduction of \$5,095 to Applicant's proposed adjustment or an adjusted lease expense of \$4,556.

(3) Applicant incurred \$1,200 during the test year in management fees. The record reflected that the charges for management services were recorded as engineering fees and that the \$1,200 fee was in addition to the actual services provided by Miller, Wihry and Lee. The Commission is of the opinion that the

management services included in the engineering expenses reflect the actual cost of management of the sewer system and that the additional \$1,200 fee charged the Applicant is unjustified. The Commission has therefore excluded the \$1,200 expense for rate-making purposes.

(4) Applicant proposed an increase of \$1,321 to the engineering expense. The adjustment reflected an estimated increase of \$321 in recurring engineering expense and \$1,000 for one-third of the rate case expenses for engineering. Actual bills submitted by the Applicant show a total rate case expense of \$2,687. Therefore, the Commission has adjusted the allowed engineering rate case expense to \$825. Also, the Commission is of the opinion that the adjustment of \$321, which was based solely on an estimated inflationary increase in cost, should not be included herein for rate-making purposes.

(5) Applicant proposed an adjustment of \$1,371 to reflect increased costs in the collection charges from Louisville Water Company. The Commission has increased this expense by \$335 to reflect the proper apportionment of the joint service cost of \$1.53, which was placed in effect on May 1, 1981, and the rates allowed herein.

(6) Applicant proposed to include income tax expense in the amount of \$6,103 based on the requested rate increase. The Commission has allowed an expense of \$6,135 for income taxes based on the revenues and expenses found reasonable herein.

(7) Applicant proposed an adjustment of \$5,822 to routine labor expense to reflect an anticipated 9% cost of living wage increase based on the previous year's experience of Rolling Hills Operating Company. the Commission is of the opinion that this increase has no substantive support in that it was based on an estimated inflationary increase in cost. Therefore, the Commission has not allowed the adjustment for rate-making purposes.

During the test year the Operating Company increased the overhead factor applied to direct labor charges from .25 to .75. This charge, along with additional hourly wage increases, increased the labor expense to the Applicant significantly. Applicant submitted a calculation of the overhead factor on June 23, 1981, per the second set of interrogatories. There were several errors in the calculation of this factor. The Commission is of the opinion that the factor is excessive and therefore, has reduced the overhead factor to .50 for rate-making purposes. This results in a reduction of \$5,901 in the test year expense. The Commission finds that the amount of overtime charged to Applicant during the test year by the Operating Company was excessive. Based on information contained in the record, Applicant was charged, in many instances, an overtime rate for employees who worked less than 40 hours per week. Therefore, we have adjusted the actual test year expense by \$766 to reflect the regular time rates for these employees.

(8) Applicant proposed an adjustment of \$1,624 to the maintenance and repair expense accounts. The Commission is of

the opinion that the adjustment is not known and measurable inasmuch as it was based solely on an estimated 10% inflationary increase in costs. Therefore it should not be included for rate-making purposes. Moreover, the Applicant included several items in the test year repairs and maintenance expenses that should be capitalized. The Commission has reduced the total repairs and maintenance expense for the bill dated November 8, 1979, of \$565.67 which represents a replacement of a burned-out motor; the bill dated January 3, 1980, of \$215.59 for a chlorinator pump; the bills dated February 12, 1980, of \$522.13 and \$2,759.93, which represent a primary pump valve and process and recirculating pump, respectively. Based on the decision that these items should be capitalized, the Commission has included an additional depreciation expense of \$769 for rate-making purposes.

During the test year, the Operating Company was charging the Applicant the highest labor rate for all repair and maintenance labor performed by it. Based on the data submitted by the Applicant concerning the actual labor costs incurred by the Operating Company, the average labor rate was much lower. The Commission is of the opinion that for rate-making purposes an average hourly rate of pay of \$7.50, including the markup allowed herein, is reasonable based on the evidence of record. Therefore, the Commission has reduced the repair and maintenance expense items by \$2,082 for rate-making purposes.

(9) The Commission has adjusted test year revenues by \$9,007 to reflect the Annual revenue based on the level of customers at the end of the test year.

Based on the allowed pro forma adjustments, Applicant's test period operations would appear as follows:

| | <u>Actual</u> | <u>Adjustments</u> | <u>Adjusted</u> |
|-------------------------|-------------------|--------------------|-----------------|
| Operating Revenues | \$179,418 | \$ 9,007 | \$188,425 |
| Operating Expenses | 185,904 | (20,776) | 165,128 |
| Operating Income (Loss) | (6,486) | 29,783 | 23,297 |
| Other Income | 2,527 | 724 | 3,251 |
| Other Deductions | 12,911 | (918) | 11,993 |
| Net Income | <u>\$(16,870)</u> | <u>\$31,425</u> | <u>\$14,555</u> |

Revenue Requirements

The Commission is of the opinion that the operating ratio⁽¹⁾ of 88% proposed by the Applicant is fair, just and reasonable and should be used in this case. It will permit Applicant to pay its operating expenses, service its debt and provide a reasonable return to Applicant's owners. Therefore, the Commission finds that Applicant is entitled to increase its rates to produce revenues of \$196,523 or an increase in revenues of \$8,098.

Summary

The Commission, after consideration of the evidence of record and being fully advised, is of the opinion and so finds that the rates proposed by Rolling Hills Service Company, would produce revenues in excess of those found reasonable herein and therefore, must be denied upon application of KRS 278.030.

The Commission further finds that the rates set out in Appendix A, attached hereto and made a part hereof, are the fair,

(1) Operating Ratio =
$$\frac{\text{Operating Expenses} + \text{Depreciation} + \text{Taxes}}{\text{Gross Revenue}}$$

just and reasonable rates to charge for sewage service rendered by Applicant in that they will permit Applicant to meet its reasonable operating expenses and to accumulate a reasonable surplus for equity growth.

IT IS THEREFORE ORDERED that the rates set forth in Appendix A, attached hereto and made a part hereof, are the fair, just and reasonable rates to charge for sewage service rendered by Rolling Hills Service Company on and after the date of this Order.

IT IS FURTHER ORDERED that the rates proposed by Applicant are hereby denied.

IT IS FURTHER ORDERED that Rolling Hills Service Company shall file with this Commission within 30 days from the date of this Order its revised tariff sheets setting out the rates approved herein.

Done at Frankfort, Kentucky, this 30th day of July, 1981.

PUBLIC SERVICE COMMISSION

Marlin M. Vohs
Chairman

Did not participate
Vice Chairman

Jim Flannery
Commissioner

ATTEST:

Secretary

APPENDIX A

APPENDIX TO AN ORDER OF THE PUBLIC SERVICE COMMISSION IN CASE NO. 7983 DATED JULY 30, 1981.

The following rates are prescribed for all customers served by Rolling Hills Service Company, Inc. All other rates and charges not specifically mentioned herein shall remain the same as those in effect prior to the date of this Order.

| <u>Customer Category</u> | <u>Monthly Rates</u> |
|---------------------------|------------------------|
| Single-Family Residential | \$ 9.50 per residence |
| Multi-Family Residential | 7.35 per dwelling unit |
| Commercial Facilities | 16.40 per R.E.* |
| Educational Facilities | 16.40 per R.E.* |
| All Other | 16.40 per R.E.* |

* Residential Equivalent = 400 gallons per day